NOTES

WASHINGTON NOTES

THE WAR REVENUE BILL

On September 3 the Ways and Means Committee reported, and on September 20 the House of Representatives passed, the so-called War Revenue Bill (H.R. 12,863, Sixty-fifth Congress, Second Session), which has been under consideration in committee for practically three months past. So complex is the measure and so lengthy its detailed provisions that only a very general summary of its effect can be furnished. In general the proposed law amounts practically to a doubling of the existing volume of internal taxation, but in many classes of the revenue now collected it will triple or quadruple the burden previously imposed. Structurally the bill is comparatively simple, providing as it does for (1) taxes on income; (2) taxes on excess profits and war profits; (3) taxes on commodities, such as beverages, automobiles, etc.; and (4) stamp and other excise taxes on various instruments, documents, etc. Basically the new normal income tax rate is fixed at 12 per cent instead of 4 per cent, with the surtaxes as in the past beginning after $5,000 and being to all intents and purposes doubled. The highest ranges of surtaxes are of course not materially altered, but they were already so high as to permit of but little advance. Exemptions remain as heretofore, while below $4,000 a reduction from the normal rate of 12 per cent to 6 per cent is provided. Whereas, therefore, the man with an income of $5,000 will pay a normal tax of 12 per cent on $1,000 of his revenue, he will pay only 6 per cent on the taxable sum below that figure. The highest ranges of income (above $5,000,000 annually) will now be taxed at practically 77 per cent, including both normal and supertax. Probably the greatest controversy has been produced by the so-called war-profits or excess-profits taxes. On these, two alternative methods of levy have now been proposed, the so-called war-profits plan calling for a rate of 80 per cent on all above a specified normal or minimum profit exemption of about 10 per cent. Beverage taxes have been enormously raised, while the duties on a long list of commodities classed as "luxuries" will inevitably add very greatly to the prices of many articles. There seems to be little reason to doubt that the new bill will produce the revenue it is intended to raise, provided that its operation does not result in curtail-

ing the income-producing power of the nation by cutting off the saving margin so largely as to cripple industrial enterprise. On this point considerable difference of opinion is already manifest, the prevailing view of the business community being undoubtedly that the effect of the bill in the direction referred to will involve very considerable danger. On the other hand, the imposition of the new income taxes at the proposed rate admittedly has an exceedingly important bearing upon the success to be expected in the placing of government loans. These loans are now being raised primarily through sales of bonds to the recipients of moderate incomes, who in a very large number of cases have subscribed as liberally as they could. In those instances where individuals are putting practically their whole savings into the purchase of Liberty bonds the new income taxes must necessarily operate to reduce the bond-buying power of the individual. Assuming that such instances are sufficiently numerous, their effect will tend to be that of reducing the power to distribute the Liberty bonds as widely as formerly, unless the purchases heretofore made by men of moderate income are practically taken over by the recipients of the higher classes of wages and by the so-called working class in general. The distribution of the bonds among this element in the community has not thus far been very successful, and it remains to be seen whether a field for the sale of the securities can be developed there. The estimated yield of the new bill may be taken as somewhere between eight and nine billions of dollars, or from two to two and one-half times the yield of present internal taxation.

MORE BOND LEGISLATION

The measure recommended by Secretary of the Treasury McAdoo on September 10 and passed by the Senate on September 18 in a form substantially identical with that in which it had previously passed the House is to be regarded as the complement to the war-revenue measure and will in future be studied in conjunction with it as embodying the complete statement of Treasury policy for the year 1918–19. This bill provides for two fundamentally important provisions: the exemption of the new bonds from taxation up to a specified amount and the establishment of the power of the Treasury Department to control foreign exchange through the acquirement of banking credits abroad as well as in other ways. The provision of the bill bearing upon the exemption of bonds from taxation, although highly complex in language, is simple in its conception. It provides for the exemption from taxation of a specified amount of Liberty bonds of the various loans so long as they are in

the hands of any one holder. The aggregate of Liberty bonds which could thus be exempted from taxation, so far as income is concerned, would apparently be \$75,000. The exempt holdings are, however, to be distributed among the several successive issues, and a substantial percentage of them must have been obtained through original subscription to the fourth Liberty Loan. Thus there is held up to the prospective subscriber the prospect of exemption for a considerable amount of income, so far at least as the taxes to be levied during the war are concerned—for it is expressly provided by the Secretary of the Treasury that at the close of the war, when the surtaxes upon income are supposedly to be reduced, the exemption from taxation shall cease. Inasmuch as the bonds are already free of all normal income tax, the exemption from surtaxes during the continuance of the war practically means that an individual may be safe in the enjoyment of about 4 to $4\frac{1}{4}$ per cent upon his money during the war, provided he is willing to put it into Liberty bonds. This course has been selected by the Secretary of the Treasury in lieu of the plan which has been urged by not a few students of the Treasury situation—that there should be an advance in the rate of interest on bonds that would carry it up to the commercial level; or else that Congress should be asked to permit the selling of bonds below par, as is the practice in foreign countries, so that the government would be paying the going rate for such advances as it may secure. The present administration of the Treasury Department has been opposed to either of these expedients, although the rate on government bonds has been advanced from $3\frac{1}{2}$ to $4\frac{1}{4}$ per cent, the Secretary's view being that every effort should be made to avoid further increases because they involve great expense to the government. The exemption from taxation brings about practically the same situation, so far as the bondholder is concerned, but the case is quite different when the relation of the interest rate on government bonds to the commercial rate of interest is considered. It is an unquestionable fact that our market rates have been held to artificially low levels, as is shown by the experience of foreign countries as well as by analytical study of our own problems. So long as the rate of interest on government bonds stands at a certain figure, it is almost out of the question to attempt to raise the commercial rate on prime paper much above that figure. To do so would be to facilitate the downward movement of the bonds in the market, and consequently the effort has been generally made to hold commercial rates at a practical parity with those paid by government securities. The proposed exemption of the bonds from taxation is the

second change of policy since the beginning of the war, the first issue of bonds having been wholly tax-exempt, while the second and third issues were given only a very limited exemption. The new plan is a compromise between the two former policies.

GOVERNMENT CONTROL OF RAILWAYS

The first formal report of the operation of railroads under government control has been furnished to the President by the Director General of Railroads in a formal document filed under date of September 3. This report reviews the experience of the railroad administration from the taking over of the roads some seven months ago up to the present time and summarizes the various changes of policy that have been effected. A portion of the report is given to the statement of analysis of economies that have been effected in the salaries of the personnel. In general the policy adopted with regard to this phase of management has been a material reduction for the higher-paid officials and an increase for the lower grades of employees, intermediate salaried officers remaining practically unchanged. Advances in wages granted since the government took over the roads have aggregated probably $400,000,000 per annum, while the savings effected in salaries have of course been very much smaller. Other savings that have been introduced are seen in the consolidation of ticket offices, the cessation of advertising, the suspension of various methods of competition, and other similar expedients. The advance in freight rates by about 25 per cent and the parallel advance in passenger rates, both of which were put into effect last June, are naturally defended on the ground that they have been necessitated by the constant increase in the cost of doing business, as well as by the increase in direct wage payments. It is shown that conditions surrounding the movement of freight are very much better now than at the time when the transfer of control occurred. The congestion which was then characteristic has been terminated, and although many classes of freight are still held up or are moving slowly, it is on account of the priority granted to war munitions and is designed to insure their prompt movement to the ports of shipment.

Financial relations between the railroads and the government are explained at length but have not yet been brought to a settled basis, owing to the fact that security holders continue dissatisfied with the form of contract proposed by the railroad administration to govern the use of the funds received from operation. There is little in the report to make a definite showing in favor of government control as a

permanent policy, for, while it is true that many economies have been introduced and some sources of waste eliminated, it would seem from the facts and figures in the case that government operation is certainly much more costly and probably much less convenient for the public than was the old régime. This conclusion itself is by no means final, because of the obvious fact that the taking over of the roads was a war measure and as such to be regarded as temporary in its effects and intended to meet a temporary condition. The situation has in fact been so abnormal during the months of government control of railways that no reasonable conclusion either way could be properly based upon the experience during that period. Time has not yet been afforded for any showing of the effect of the increased rates upon the earnings of the roads, for the enlarged receipts during the first few months of operation were absorbed almost immediately in the payment of back wages under the award made by the board which investigated the wage situation and acted upon by the Secretary of the Treasury. The most recent reports of earnings show a gratifying increase. The fact still remains that in raising rates the government took a step which has been strongly urged by the railroads, and that, had they been given the larger income which they then asked, they would have been able to supply correspondingly better facilities—perhaps in a degree that would have rendered it unnecessary or undesirable to attempt a system of public operation.